April 24, 2025

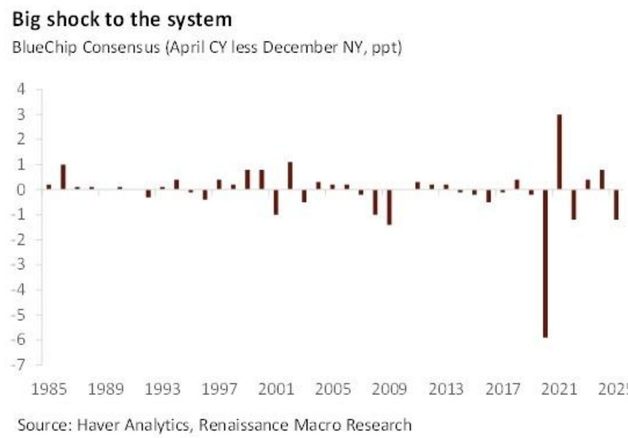
Dutta's Economic Daily

Consensus has been surprised

Neil Dutta

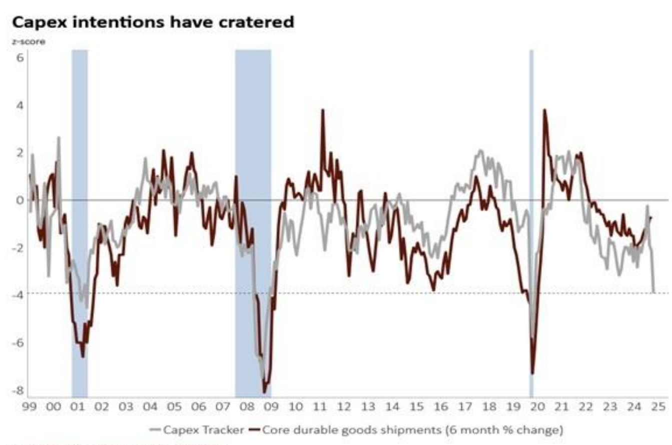
Talk about a rug pull

- One of the ways a recession works is through an element of surprise. Households and businesses think conditions will be okay and then, all of sudden, they aren't. One day, you are gearing up for the growth and the next, you are clearing out inventories, investing and hiring. To that end, see our nearby figure. Here is what it shows. I take the current year Q4 GDP estimate, as of April, and see the change relative to what the consensus saw in December of the previous year. So, the latest Bluechip Estimate has Q4 2025 growth at 0.7%. In December, it was 1.9%. That's a 1.2ppt decline. Go back in history outside of the COVID years and the last time we saw anything like this was 2009.



Durables helped by aircraft

- Durable goods orders surged 9.2% in March thanks to a 139% increase in nondefense aircraft and parts orders. Excluding transportation, durable goods orders were flat. Nondefense capital goods ex aircraft orders rose 0.1% following a 0.3% decline the month prior. Core orders were led by primary metals and communications equipment – tariff front running? Core shipments advanced 0.3% following a gain of 0.7% in February. The growth in core shipments was helped by primary metals; excluding this, core shipments would have declined. So, there was not much going on. Stepping back, the broader story now is that six-month capex intentions have collapsed. Expect core durables to soften in the second quarter.



Assessing China's economic resilience

- A recent NY Fed article provides a careful assessment of China's economy as it navigates a complex landscape marked by a struggling property sector and escalating trade tensions with the U.S. The property crisis, initiated by tightened borrowing requirements in 2020, led to the default of major developers like Evergrande and a ripple effect across related industries. This downturn has resulted in a 60% drop in property sales, a 70% decline in new construction starts, and a 20% decrease in active construction floor area. Property prices, despite government intervention, have fallen by 16%.

- China's response has been marked by forceful, albeit intermittent, stimulus measures. These include interest rate cuts, reductions in banks' reserve requirements, increased government spending, relaxed restrictions on home purchases, and accelerated investment in industry and infrastructure. Despite these efforts, the effectiveness of the stimulus remains uncertain due to opaque fiscal practices and questions surrounding the accuracy of official economic data. While fixed asset investment in manufacturing and infrastructure has reached multi-year highs, offsetting the contraction in real estate investment, and contributing to a near $1 trillion trade surplus, the overall growth picture is less clear. Alternative estimates, incorporating a wider range of data, suggest that GDP growth, while positive, has been slower than official figures indicate.

- A key constraint on growth is the limited fiscal space at the local government level. The IMF estimates augmented local government debt at a staggering 93% of GDP, a 60 percentage point increase over the past decade, driven by average deficits of 10% of GDP. While the government has acknowledged the issue and initiated debt restructuring for local government financing vehicles (LGFVs), the tightening of local government finances has limited the impact of stimulus.

- Given these complexities, aggregate credit growth serves as a valuable indicator of policy stance. The "credit impulse," the change in new credit relative to GDP, has been more subdued than in previous cycles, reflecting a more cautious approach to local government borrowing. However, a strong correlation exists between credit impulses and GDP growth. A shift to a "moderately loose" monetary policy, potentially returning credit growth to 2023 levels, could generate a substantial credit impulse, boosting GDP growth by 0.5 to 1 percentage point. This, however, risks reinforcing China's dependence on industrial-led growth at the expense of a much-needed shift towards consumption.

Some observations in earnings calls

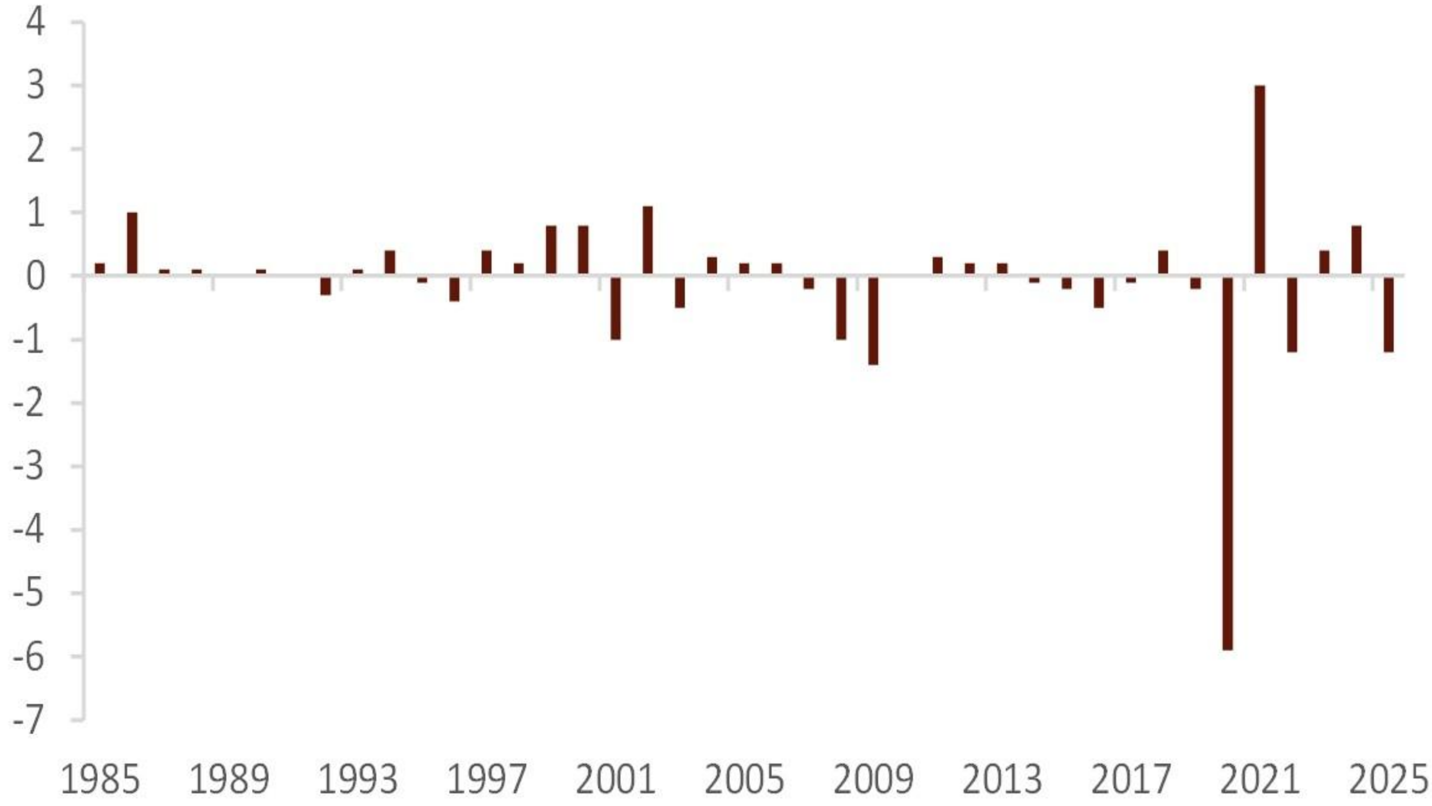
- $RHI: Business confidence levels moderated during the quarter in response to heightened economic uncertainty over U.S. trade and other policy developments. Clients and job seeker caution continues to elongate decision cycles and subdue hiring activity and new project starts.

- $MHO: As we began 2025, it was clear to us that rate buy-downs remain necessary for us to drive traffic and promote sales, and that such rate buy-downs would continue throughout the spring selling season, unless and until it became clear that consistent and solid demand had returned. Clearly, that has not happened. Instead, what we have seen is the continuation of choppy and challenging conditions.

- $CMG: In February, we began to see that the elevated level of uncertainty felt by consumers starting to impact their spending habits. We could see this in our visitation study, where saving money because of concerns around the economy was the overwhelming reason consumers were reducing the frequency of restaurant visits. This drove a slowdown in our underlying transaction trends, this trend has continued into April.

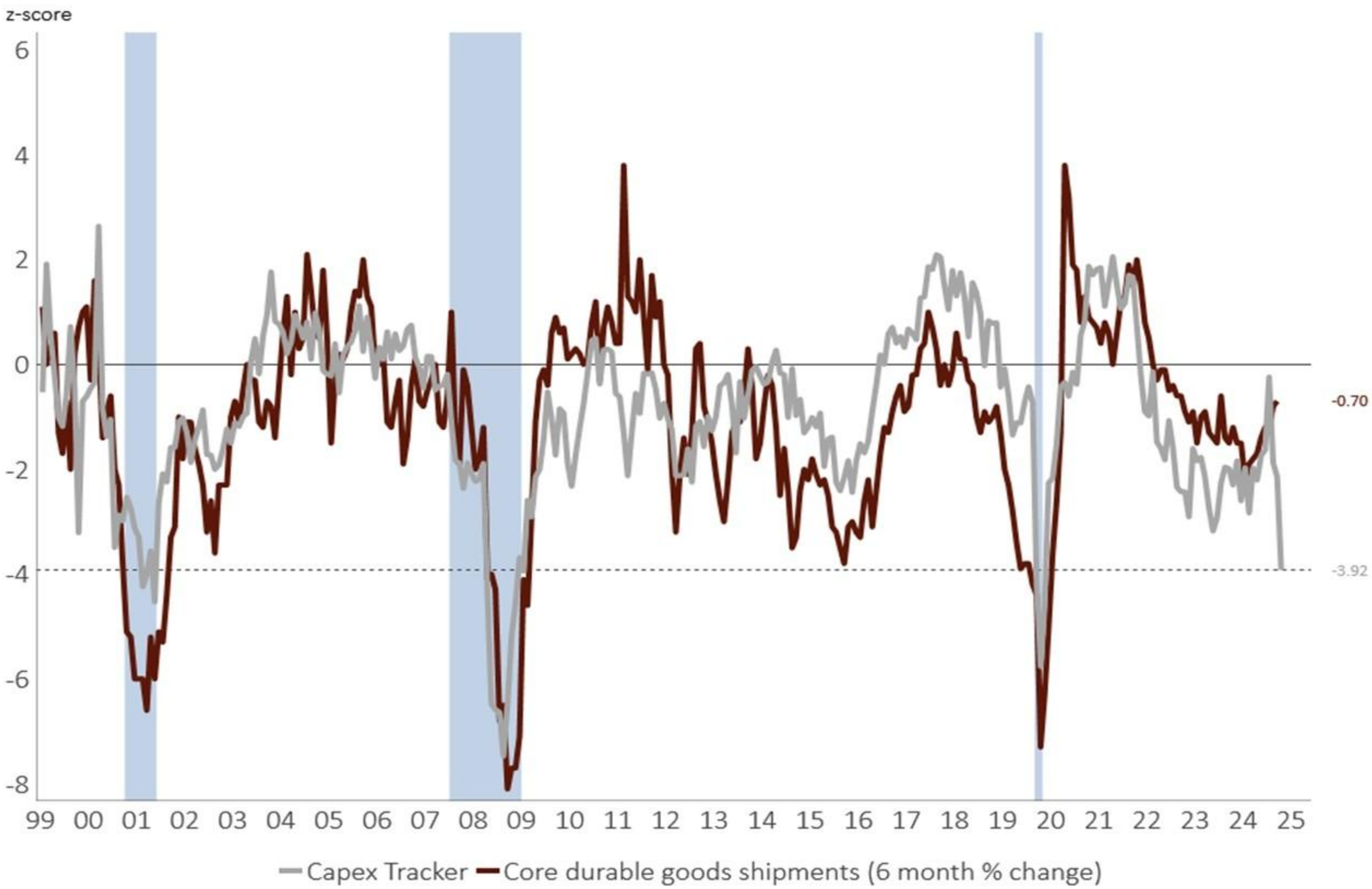
Big shock to the system

BlueChip Consensus (April CY less December NY, ppt)



Source: Haver Analytics, Renaissance Macro Research

Capex intentions have cratered



Source: Renaissance Macro Research, Macrobond